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IN THE

Supreme Court of the United States

OCTOBER TERM, 1993

STUART K. PATRICK,

Petitioner,

—v.—

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

PETITION FOR A WRIT OF CERTIORARI

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Questions Presented

1. Was Petitioner denied his constitutional right to due process when he was convicted on appeal of a different charge from the one asserted against him by the New York Stock Exchange, after having been unanimously exonerated of that charge in the hearing at the Exchange?

2. Did the Court of Appeals improperly confuse the role of the Securities and Exchange Commission as the appellate reviewer of decisions of the New York Stock Exchange with the SEC's role in connection with disciplinary proceedings conducted by the SEC itself, and thereby undermine and frustrate the appellate review intended by Congress for disciplinary proceedings of self-regulatory bodies such as the Exchange?

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Opinions Below

The Hearing Panel of the New York Stock Exchange, which conducted the trial in this proceeding, rendered an opinion dated April 11, 1991, exonerating Petitioner, which is reproduced in the Appendix at A 28a - 31a. The opinions of the Board of Directors of the Exchange dated March 5 and May 7, 1992, reversing the decision of the Hearing Panel are contained at A 27a and A 22a - 23a. The opinion of the Securities and Exchange Commission dated May 17, 1993, sustaining the sanctions imposed by the Exchange Directors is contained at A 8a - 20a. The opinion of the United States Court of Appeals for the Second Circuit dated January 19, 1994 and

published March 22, 1994, denying Petitioner's petition for a review of the SEC's decision, is contained at A 1a - 7a. Petitioner is not aware of any official reports (to date) of any of those opinions.

Jurisdiction

The judgment of the Court of Appeals was entered on January 19, 1994. There was no petition for re-hearing. This Court has jurisdiction to review the judgment of the Court of Appeals by writ of certiorari pursuant to 28 U.S.C. § 1254(1).

Constitutional and Statutory Provisions Involved

This case involves the Due Process Clause of the Fifth Amendment to the United States Constitution, which provides that "[n]o person shall be . . . deprived of life, liberty or property, without due process of law." This case also involves §§ 19(d)(2) and 25(a)(1) of the Securities Exchange Act of 1934 [15 U.S.C. §§ 78s(d)(2) and 78y(a)(1)], which provide for review by the Securities and Exchange Commission of final disciplinary sanctions imposed by the New York Stock Exchange as a self-regulatory organization [§ 19], and further review by the United States Court of Appeals from final orders of the SEC on such a review [§ 25]. Those statutory provisions are printed in the Appendix at A 39a - 40a, since they are lengthy. Exchange Rules 342(a) and 342(b), which are also applicable to this Petition, are printed at A 38a.

Statement of the Case

the parties

Petitioner, Stuart K. Patrick ["Patrick"] was and is the President of Baird, Patrick & Co., Inc. ["Baird Patrick"], a long-standing, reputable securities broker-dealer which is a mem-

ber of the New York Stock Exchange and is located in New York City.

Baird Patrick, as a registered broker-dealer is subject to the regulatory scheme created by Congress in the Securities Exchange Act, including regulation by the Exchange and the Securities and Exchange Commission.

the Exchange disciplinary charges

Christian Keller, a Vice-President of Baird Patrick, committed certain violations on the floor of the New York Stock Exchange in connection with his trading in a firm proprietary account, for which violations the Exchange disciplined both Mr. Keller and Baird Patrick.

Thereafter, on August 29, 1990, the Exchange's Division of Enforcement issued a Charge Memorandum [A 32a - 34a] against Mr. Patrick, charging that he had violated Exchange Rule 342(a) by failing to "reasonably discharge his duties and obligations in connection with the supervision and control of the activities of an employee or employees under his supervision" [A 34a], viz. Mr. Keller. Specifically, the charge asserted that Mr. Patrick was "a direct supervisor of [Mr. Keller] and was responsible for supervision of Keller's trading" in the firm proprietary account [A 33a, ¶ 11].

In response, Mr. Patrick denied that he had committed any wrongdoing, and specifically that he was Mr. Keller's direct supervisor and was responsible for supervision of Mr. Keller's trading [A 35a - 37a].

the Exchange Hearing Panel decision

On April 11, 1991, a hearing on the charge was held before an Exchange Hearing Panel, at which several witnesses testified and documentary evidence was submitted to the Hearing Panel. The evidence showed that Mr. Patrick, who was located at Baird Patrick's executive offices on Wall Street, several blocks away from the Exchange's trading floor, was

not the supervisor of floor trading for the firm, and was not the supervisor of Mr. Keller's activities on the floor. Indeed, the witnesses at the hearing unanimously so testified, without contradiction by the Exchange's Division of Enforcement.

The Exchange Hearing Panel unanimously exonerated Mr. Patrick of the charge on April 11, 1991 [A 28a - 31a]. The Hearing Panel found that Mr. Patrick was not Mr. Keller's supervisor, and therefore was not guilty of the charge against him under Exchange Rule 342(a), even though the firm (at which he was the President) had failed to implement appropriate supervision of Mr. Keller's floor trading activities.[1] Indeed, the Hearing Panel held that it "cannot find, on the evidence presented in this case, that [Mr. Patrick] in fact had reason to believe he bore direct responsibility over the firm's trader during the relevant period" [A 31a].

the Exchange Directors' decision

The Exchange's Division of Enforcement appealed from the Hearing Panel decision to the Exchange's Board of Directors. A panel of the Directors reversed the Hearing Panel decision on March 5, 1992, and held that Mr. Patrick had violated Exchange Rule 342(a) [A 27a]. As a result, it directed that he be censored and suspended for one week from employment or association in a supervisory capacity with any member firm [*id.*]. Initially, the Directors gave no reasons for its decision [A 27a].

Mr. Patrick duly appealed that decision to the SEC. The SEC, finding the Directors' decision inadequate, directed that the Exchange's Directors supplement their decision [A 25a]; and the Directors did so in a supplementary decision on May

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[1] The firm had relied upon Mr. Keller (as an officer) to supervise floor trading, and thus had failed to establish additional supervision of floor trading. As previously noted, Mr. Keller and the firm (Baird Patrick) were both sanctioned for Mr. Keller's wrongdoing. That lapse by the firm was corrected promptly thereafter.

7, 1992 [A 22a - 23a]. There, the Directors reasoned that Mr. Patrick had violated Rule 342(a) because, as president and chief executive officer of the firm, it was Mr. Patrick's responsibility "to assure that the firm's management structure provided for such supervision" [A 23a].[2] That, however, was not part of the charge against him [cf. A 32a - 34a].

the SEC decision

After briefing to the SEC, the SEC entered an order on May 17, 1993, sustaining the disciplinary action against Mr. Patrick and the sanctions imposed upon him [A 8a - 21a]. The SEC concluded that Mr. Patrick, "as Chief Executive Officer and President of [Baird Patrick], had overall responsibility for the firm's operations" [A 10a] and that, as Mr. Keller's "direct *superior*" [A 11a], Mr. Patrick had violated Exchange Rule 342(a) because he had "failed to assign any responsibility for assuring Keller's compliance with the floor trading rules" [*id.*].[3]

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[2] The Directors also stated that "the evidence established that [Mr. Patrick] exercised supervisory responsibility over certain of the trader's activities" [A 22a]. This apparently referred to testimony that, when Mr. Keller wished to hold securities in the firm's proprietary account overnight, he would discuss that financial question with Mr. Patrick before doing so, so that there would be no adverse impact on the firm's required capital. However, that was not evidence that Mr. Patrick supervised Mr. Keller's *trading* activities on the floor of the Exchange, which were the only activities at issue in the Keller/Baird Patrick disciplinary proceedings and the disciplinary proceeding against Mr. Patrick.

[3] As can be seen from a reading of Exchange Rule 342(a) and Exchange Rule 342(b) [reprinted in the Appendix at A 38a], Rule 342(b), *not* Rule 342(a) requires that a firm's partners or directors "provide for adequate supervisory control" and designate "a general partner or principal executive officer to assume overall authority and responsibility for internal supervision and control". Rule 342(b) also requires that the designated person "establish a separate system of follow-up and review" to assure that employees are adequately supervised. Mr. Patrick contended, and contends here, that he has been found guilty on appeal of violating Rule 342(a) on the basis of responsibilities under Rule 342(b)—a rule and responsibilities which he was never charged with having violated.

the Court of Appeals decision

On July 13, 1993, Mr. Patrick petitioned the United States Court of Appeals for the Second Circuit, seeking a reversal of the SEC's order and reinstatement of the Exchange Hearing Panel's decision exonerating him. The Court of Appeals had jurisdiction to hear and decide that petition pursuant to § 25(a)(1) of the Securities Exchange Act [15 U.S.C. § 78y(a)(1)], which allows a person "aggrieved by an order of the SEC to obtain a review thereof in the United States Court of Appeals for the circuit in which he resides or has his principal place of business"; Mr. Patrick's principal place of business is within the Second Circuit.[4]

On January 19, 1994, the Court of Appeals denied Mr. Patrick's petition and sustained the SEC's order sanctioning Mr. Patrick [A 1a - 7a]. The Court of Appeals held that, since "as president, Patrick was 'in charge' of all the employees in the firm", he was necessarily responsible for supervision of Mr. Keller's activities unless he had himself delegated that function to someone else or knew that someone else was performing that function [A 6a]. In doing so, the Court of Appeals cited and relied upon two decisions of the SEC involving disciplinary proceedings brought by the SEC itself, not proceedings under Exchange Rule 342(a) or otherwise brought by the Exchange's Division of Enforcement.[5] Mr. Patrick is now petitioning this Court for a writ of certiorari with respect to that decision.

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[4] On his application, the penalties imposed against Mr. Patrick have been stayed pending his appeals.

[5] Moreover, the only cases with respect to Exchange Rule 342 cited on behalf of the Division of Enforcement referred to consent decrees, not contested proceedings where this issue was ever actively litigated.

Reasons for Granting the Petition

1. The issues are important

This case presents important constitutional and statutory questions. These include: [a] the right of a person to obtain a fair and meaningful review of a disciplinary action by a self-regulatory securities exchange; [b] the appropriate role of the SEC (as the oversight agency specified by Congress for such review) and, thereafter, by the Courts of Appeals (which Congress specified as the reviewing authority for such decisions of the SEC); and [c] the responsibility and potential liability of the president of a corporation merely because he holds that office (a matter governed by state law, but legislated by the SEC's decision here).

Review by this Court is necessary not only to correct a serious injustice, but also to assure that Congress's intention in creating a system of appellate review is not rendered nugatory; i.e., to delineate the appropriate appellate responsibilities of the SEC and the Courts of Appeals when reviewing disciplinary proceedings of self-regulatory organizations. These matters are also important because the decisions below set an important precedent, and have serious societal and economic implications with respect to civil disciplinary proceedings in general, and for the highly-regulated securities industry and the legitimate expectations and responsibilities of corporate officers.[6]

2. Petitioner's right to due process was plainly violated

After having been exonerated of the only charge made against him, Mr. Patrick was found guilty on appeal of committing wrongdoing which was never charged against him and is not specified in the only Exchange Rule cited in the Charge Memorandum against him (i.e., Rule 342(a)). Mr. Patrick con-

[6] Indeed, the SEC itself, in convincing the Court of Appeals to publish its opinion, emphasized the precedential nature and effect of the decision at issue [A 41a - 43a].

tends (and contended before the SEC and the Court of Appeals) that his constitutional right to due process prohibits his being convicted on appeal of a charge which was never made against him below and which he was never required to defend himself against at his trial (i.e., the Exchange hearing). See, e.g., *U.S.* v. *Baker*, 807 F.2d 1315, 1323-24 (6th Cir. 1986).

On the appeal to the SEC, the SEC broadened the charge to refer to Mr. Patrick's role as Mr. Keller's direct *superior* (as opposed to supervisor); and it blended or legislated responsibilities provided for in Rule 342(b) into Rule 342(a) [see, e.g., A 13a - 15a]. As Mr. Patrick showed, when the Exchange intends to charge an individual with violating both Exchange Rule 342(a) and Exchange Rule 342(b), it had so specified in its Charge Memorandum, mentioning both such rules and delineating the allegedly wrongful conduct under both such rules. That was not done here.

Even if the Court agrees with the SEC and the Court of Appeals that Mr. Patrick's supposed responsibilities as a corporate "superior" are implicit in Exchange Rule 342(a), a proposition with which Petitioner respectfully disagrees, that does not alter the impropriety of the procedure applied against Mr. Patrick, since the Charge Memorandum was limited to Mr. Patrick's supposed role as Mr. Keller's direct *supervisor* (*not superior*) and the supposed supervisor's role with respect to Mr. Keller's trading activities on the Exchange floor. Mr. Patrick successfully defended himself against that charge at the hearing.[7] Mr. Patrick was not called upon to defend himself against the charge first raised on the appeal from the Hearing Panel Decision, i.e. that his position as pres-

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[7] The Hearing Panel's findings in this regard are entitled to special deference on appeal, since it was the Hearing Panel, not the appellate bodies, which heard the witnesses (including Messrs. Patrick and Keller, the two persons directly involved), observed their demeanor, and otherwise had the duty of weighing the evidence as it was presented. See, e.g., *Anderson* v. *Bessemer City*, 470 U.S. 564, 573-75 (1985).

ident of the firm and vis-a-vis Mr. Keller in the corporate structure imposed other and different duties with respect to the supervision of Mr. Keller (viz., a supposed duty to assure that Mr. Keller had some supervision). That, Petitioner respectfully submits, is a responsibility under Exchange Rule 342(b), not Exchange Rule 342(a); however, regardless of that fact, it was improper to confront Mr. Patrick with such a new charge on appeal, after the trial was over.

If left standing, the decision below will mean that persons charged with violation of a specific Exchange rule (in a disciplinary proceeding before a self-regulatory organization such as the Exchange) will always risk conviction on appeal—after prevailing at the hearing on the specific charge—on the basis of new matters, arguments, responsibilities and even rules not included in the charge, which they were called upon to defend at the hearing. That, we respectfully submit, violates the most basic requirements of the Due Process Clause of the Fifth Amendment, and indeed the concept of basic fairness which underlies our judicial system.

3. The Court of Appeal's decision undermines Congress' intent

When Congress created the appellate structure for review of disciplinary decisions of self-regulatory organizations such as the Exchange (as prescribed in the Securities Exchange Act), it necessarily intended that such appellate review would be meaningful and fair, in accordance with the Fifth Amendment of the United States Constitution. We respectfully submit that the decisions below undermine and frustrate Congress's intent in that regard.

First, by allowing an appellate reviewing authority to change the grounds for a supposed conviction and depart from the Charge Memorandum, the decisions below deprive an individual of his right to a fair trial of the charge against him. The contention that the supposed responsibilities which the

Court of Appeals held Mr. Patrick violated are implicit in Rule 342(a) is not a sufficient justification for the appellate reviewers' departure from the specific and limited Charge Memorandum which Mr. Patrick was called upon to defend himself against at the hearing. The Charge Memorandum did not charge Mr. Patrick with violating Rule 342(a) on the basis of those other supposed duties. By contrast, the Exchange Hearing Panel correctly addressed itself to the specific charge against Mr. Patrick. Thus, the Hearing Panel rendered the appropriate decision with respect to the Charge Memorandum, which stated the *only* charge that Mr. Patrick defended himself against, and was called upon to defend himself against.

Second, the Court of Appeals confused the role of the SEC as a reviewing body with its separate and different role as a disciplinary body. Here, the SEC is called upon solely to review the disciplinary decision of the Exchange. The SEC itself had not brought any disciplinary action against Mr. Patrick, and its disciplinary procedures and the precedents with respect to its own disciplinary proceeding were not at issue. The SEC ignored its appellate responsibility and, instead, legislated into Exchange Rule 342(a) its view of what that Rule *should* provide (i.e., the supposed responsibility of a corporate "superior"), which is not contained in that rule. That was improper; it conflicted with the role which Congress gave to the SEC in this situation; and it further deprived Mr. Patrick of his constitutional right to due process.

The Court of Appeals compounded this error by relying upon two decisions of the SEC which have nothing to do with Exchange Rule 342(a), but rather disciplinary actions by the SEC's own enforcement branch. Those decisions are not appropriate interpretations of Exchange Rule 342(a). Had the SEC's enforcement authorities brought proceedings against Mr. Patrick, he would have defended himself against the standards set forth in those decisions; however, that never happened. The only body which asserted a charge against Mr. Patrick was the Exchange, and it did so on the limited

grounds specified in the Charge Memorandum, with specific reference to Rule 342(a) and only that rule. It was improper for the SEC, particularly as appellate reviewing authority, to go beyond that rule and act as prosecutor (e.g., by, in effect, re-writing the charge against Mr. Patrick). It was also improper for the Court of Appeals to justify the SEC's decision by reference to such authorities, as opposed to authorities under or with respect to Exchange Rule 342(a).

Conclusion

For the foregoing reasons, the Petition for a writ of certiorari should be granted.

Dated: April 19, 1994
New York, New York

Respectfully submitted,

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